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1 UNITED STATES DISTRICT COURT
2 SOUTHERN DISTRICT OF NEW YORK

3 -----x
4 SECURITIES AND EXCHANGE
5 COMMISSION,

6 Plaintiff,

7 v.

19 CV 9439 (PKC)

8 TELEGRAM GROUP, INC., et al.,

9 Defendants.
10 -----x

11 New York, N.Y.
12 October 18, 2019
13 10:30 a.m.

14 Before:

15 HON. P. KEVIN CASTEL,

16 District Judge

17 APPEARANCES

18 SECURITIES AND EXCHANGE COMMISSION

Attorneys for Plaintiff

19 BY: KEVIN McGRATH
20 JORGE TENREIRO
21 DAPHNA WAXMAN

22 SKADDEN, ARPS, SLATE, MEAGHER & FLOM

Attorneys for Defendants

23 BY: ALEXANDER DRYLEWSKI
24 SCOTT MUSOFF
25 CHRISTOPHER MALLOY

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1 (Case called)

2 THE COURT: Good morning, good to see you all.

3 First question for the plaintiff is since my order of
4 late yesterday, have any agreements been reached?

5 MR. TENREIRO: Good morning again, your Honor, thank
6 you. Yes, we have been in conversations with counsel for the
7 defendants since your order of yesterday.

8 We believe we have an agreement at least with respect
9 to a schedule for conducting a hearing in this case and perhaps
10 a trial. We also believe that we have an agreement that we
11 will continue to engage in as expedited discovery as possible,
12 and I think we have an agreement there should be what I think
13 in the Court's order was called a standstill, but there seems
14 to be some disagreement from the defendants between us as to
15 whether the defendants need to continue to be enjoined until
16 the resolution of this case.

17 And their hesitance to want to be enjoined while we
18 resolve this matter completely gives us some concern, because
19 on the one hand they're telling us that they don't plan to do
20 something, but on other hand they're telling us that they don't
21 want to be under a court injunction. So I think that is the
22 biggest remaining issue of disagreement amongst the parties.

23 THE COURT: All right. Talk to me about the proposed
24 schedule and the like.

25 MR. TENREIRO: Yes, your Honor. So there is a slight

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1 disagreement between the parties as to whether this case can be
2 fully resolved as a legal matter or not, and we certainly
3 don't -- it's a little bit difficult for us to tell whether
4 there will be factual disputes as to what occurred in the past
5 or not. But assuming that we can get to some sort of list of
6 stipulation of facts, we would propose what we have been
7 calling amongst ourselves sort of a joint PI/summary judgment
8 hearing.

9 THE COURT: Well, I call it something different than
10 that, because in non-jury cases summary judgment is an
11 extremely inefficient tool. You're going to have to put your
12 direct testimony in by affidavit for the preliminary injunction
13 hearing. You will have to do that for the trial as well. And
14 that's not a summary judgment procedure at all, that's a trial.

15 MR. TENREIRO: Your Honor, that's correct, and we want
16 to have a jury trial, so we requested a jury trial.

17 THE COURT: Of what issue?

18 MR. TENREIRO: The issue of whether these are
19 securities or not might require a resolution of fact as to what
20 they told people they could expect from these investments.

21 THE COURT: And that's, in your view, not an issue of
22 law, that's an issue of fact?

23 MR. TENREIRO: It depends on whether there's a dispute
24 as to the facts. If they dispute that they told people you can
25 expect this or that from this purchase, then yes, a jury has to

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1 resolve that factual dispute. If we get to a point where
2 there's no dispute as to those facts, then yes, it's a purely
3 legal question.

4 THE COURT: Let me find out from the defendants, first
5 off, if this is a case that should be tried to a jury.

6 MR. DRYLEWSKI: Good morning, your Honor. Alex
7 Drylewski for the defendants.

8 Our position is no. The case law in this area is
9 clear, Judge Castel, that the issue of whether an instrument is
10 a security under the Howey Test, which is the test that both
11 parties agree applies here, is a legal one. And in fact, we
12 have some case law saying that in the context of a civil
13 suit -- I'm quoting from a case called *SEC v. Thompson* (10th
14 Cir. 2013), "In the context of a civil suit, the ultimate
15 question of whether an instrument is a security is a question
16 of law and not of fact, such that submitting the question to a
17 jury was error."

18 So what we proposed to the SEC is let's have one
19 hearing, we can call it a preliminary injunction and summary
20 judgment hearing, where if your Honor would like to hear
21 evidence or receive affidavits of testimony, we can provide
22 that, but the parties will also brief in advance whether or not
23 this legal question can be resolved in one side's favor or
24 whether it's the other side's favor.

25 Now we asked for a bench trial. The SEC has said that

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1 it will not consent to a bench trial, it wants a jury trial.

2 THE COURT: All right. Thank you.

3 Is that correct, the SEC will not consent to a bench
4 trial in this case?

5 MR. TENREIRO: That is correct, your Honor.

6 THE COURT: Okay. So how do you respond to the cited
7 case that suggests that it is error to submit the question of
8 whether an instrument is a security to a jury?

9 MR. TENREIRO: Your Honor, I would cite to *SEC v.*
10 *Jensen* from the Ninth Circuit, the citation is 835 F.3d 1100,
11 where the Ninth Circuit said that it was reversible error for
12 the district court to not permit the SEC to have a jury trial
13 because the SEC had brought claims for disgorgement and civil
14 penalties, as we have here.

15 THE COURT: Let's take a look at that. I take it, by
16 citing that case you concede there is no Supreme Court or
17 Second Circuit precedent on the issue.

18 MR. TENREIRO: Not that I'm aware of, your Honor.

19 THE COURT: So 835 F.3d 1100.

20 Maybe I'm misreading this, but this stands for the
21 proposition that there are claims in which the SEC is entitled
22 to a jury trial, right?

23 MR. TENREIRO: Correct.

24 THE COURT: I think that's right. I agree with that.
25 That's not the question we're discussing.

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1 MR. TENREIRO: Your Honor, the point that --

2 THE COURT: So that case, do you agree, it does not
3 address whether the SEC is entitled to a jury trial on the
4 question of whether an instrument is a security, correct?

5 MR. TENREIRO: Your Honor, I think the case stands for
6 the proposition that the district court should be careful in
7 not depriving a civil litigant the right to jury trial if they
8 have made the demand for a jury trial. We agree, I think
9 perhaps --

10 THE COURT: Why don't you answer the question that I
11 asked.

12 MR. TENREIRO: We agree that if there --

13 THE COURT: No, why don't you answer the question that
14 I asked.

15 MR. TENREIRO: That case does not stand for the
16 proposition that a Howey question has to be, or not, submitted
17 to a jury.

18 THE COURT: Okay. I thought you were citing it to me
19 for that proposition.

20 MR. TENREIRO: I apologize, your Honor. I was trying
21 to explain that our position is that if there are no actual
22 factual disputes, then absolutely the Court can and should
23 decide the question of Howey as a matter of law.

24 At this stage in the litigation, though, we don't know
25 that that will be the case, because the Court's application of

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1 law always turns on what the underlying facts are, and if the
2 defendants say certain things to the market and to potential
3 investors, that colors the Court's analysis of what a
4 reasonable investor should or should not have expected from the
5 purchase of Grams.

6 THE COURT: I hope you will promise me that if I grant
7 you a preliminary injunction you won't turn around and change
8 course and say now I don't want a jury.

9 MR. TENREIRO: It really, your Honor, depends on
10 whether there's disputes of facts, that's all.

11 THE COURT: No, but you're taking this position now
12 and for all time, you don't want a jury in this case, correct?

13 MR. TENREIRO: Well, we're taking the position that we
14 would like a jury.

15 THE COURT: You want a jury in this case in all
16 respects, you're not going to back off that position two months
17 from now, is that correct?

18 MR. TENREIRO: That's correct, only on factual
19 disputes.

20 THE COURT: That's what I wanted to know. That's what
21 I wanted to know. Thank you.

22 So tell me the schedule that you're proposing.

23 MR. TENREIRO: So we were proposing January 20 for a
24 hearing before the Court in which any purely legal questions as
25 which there are no factual disputes may be resolved.

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1 THE COURT: Say that again?

2 MR. TENREIRO: A hearing before the Court at which any
3 purely legal questions as to which there are no factual
4 disputes may be resolved.

5 THE COURT: I got a question for you: Why would I
6 need a hearing for that?

7 MR. TENREIRO: I'm sorry?

8 THE COURT: Why would I need a hearing for that?

9 MR. TENREIRO: We think we need a preliminary
10 injunction hearing because we have made a showing that there is
11 likelihood of success on the merits. The defendants would like
12 to submit the question to the Court, and we are agreeing to
13 that proposal based on their request.

14 THE COURT: So what would I hear at such a hearing?

15 MR. TENREIRO: I think, your Honor, respectfully, I
16 believe that's a question for the defendants. We want to
17 present at that hearing our showing of likelihood of success on
18 the merits and an entitlement to a preliminary injunction.

19 THE COURT: But I thought you just told me something
20 else, that would be a hearing at which you would present
21 whatever it was that could be decided as an issue of law. I'm
22 paraphrasing, but that's what I understood you to be saying.

23 MR. TENREIRO: That's correct, your Honor.

24 THE COURT: So there's no evidence to be taken on
25 that, correct?

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1 MR. TENREIRO: We would present evidence that entitles
2 such a preliminary injunction. The defendants seek to present
3 evidence to the Court at a hearing and have the Court, based on
4 that evidence, issue a ruling on the entire merits of the case.
5 We believe that that's called a motion for summary judgment,
6 and --

7 THE COURT: Well, but what you're advocating, and I
8 understood you and the defendants were agreeing that on this
9 January 20th proposal -- and I should mention that that's not
10 available, in fact I have a jury trial that week, but that's a
11 small problem, I will take care of finding an appropriate date.

12 But what I'm not getting is why you would call it a
13 hearing if it's for the Court to decide only a legal issue and
14 none other.

15 MR. TENREIRO: Your Honor, if I may take a step back.
16 If the defendants are enjoined, as we requested and as we
17 believe we're entitled to, they're enjoined from violating
18 Section 5 for the remainder of the litigation, then we can
19 have -- I wouldn't call it a hearing, I would call it a summary
20 judgment or oral argument, and the Court would not take
21 evidence, it would only look at undisputed facts, and that's
22 what we would call it.

23 THE COURT: And that's what you're proposing for
24 January 20.

25 MR. TENREIRO: Not quite, because the defendants are

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1 not agreeing to be enjoined for the rest of the litigation, so
2 that's the problem, but if we --

3 THE COURT: But that's not part of the agreement then.
4 Just confine yourself to what is part of the agreement.

5 MR. TENREIRO: The agreement would be that at that
6 date we get to present our case for a preliminary injunction
7 and they get to argue that they're entitled to summary
8 judgment. That's the agreement we have reached.

9 THE COURT: And you're not going to move for summary
10 judgment?

11 MR. TENREIRO: We haven't decided. We might
12 simultaneously move for summary judgment. It's too soon for us
13 to know.

14 THE COURT: And what would be the course of expedited
15 discovery?

16 MR. TENREIRO: The course of expedited discovery would
17 be along the lines of what we have in the order to show cause,
18 which we would attempt in good faith to -- we have already been
19 talking about meeting and conferring on some of these issues,
20 we would have some depositions and document discovery over the
21 course of the next couple of months, and we would submit to the
22 Court the undisputed facts for resolution of legal issues.

23 THE COURT: All right. Let me hear from the
24 defendants.

25 MR. DRYLEWSKI: Thank, your Honor, Alex Drylewski for

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1 the defendants again.

2 We think that this hearing should be akin to a summary
3 judgment argument. We are confident at this point, and we
4 suspect strongly there will be no issues of fact. And this is
5 again a legal issue that the case law is clear, the Howey Test
6 is a legal question that this Court can decide without taking
7 any evidence.

8 So we have been talking about putting together a
9 schedule where we will seek and give expedited discovery in aid
10 of that hearing and in advance of that hearing that we hope to
11 do by mid January, if your Honor's schedule permits.

12 In terms of the discovery deadlines themselves, what I
13 hear counsel for the SEC saying is it would like the same
14 emergency deadlines to remain in effect in this case, which
15 were under your Honor's order that was entered last Friday, I
16 believe three days for document productions and four days for
17 deposition witness production. We would like to go back and
18 meet and confer. This is the first we're hearing that this is
19 what they would like the discovery schedule to look like. We
20 would rather meet and confer and come up with reasonable
21 timelines for that.

22 THE COURT: Okay. Now talk to me about the
23 standstill. I think I understand the bid and the asked on
24 this, and let me hear from the SEC on this. Your understanding
25 is that the defendant is looking for paragraph one of its

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1 proposed order, which reads "Plaintiff's request for a
2 preliminary injunction is hereby denied without prejudice."
3 That's what you're objecting to, is that correct?

4 MR. TENREIRO: Your Honor, thank you, that is correct.
5 We're also objecting to the standstill only lasting for five
6 months and then us having to come back.

7 THE COURT: Understood. Thank you. It seems to me
8 that the way to do this, there are a number of moving parts,
9 they're not novel or unusual moving parts, they're the everyday
10 thing of what goes on in this courthouse. But what I see is an
11 order that lays out the expedited discovery, a schedule, a
12 reasonable schedule with reasonable deadlines for production of
13 documents and depositions and for briefing, and then it can
14 recite in that same order that upon the agreement of the
15 parties, defendant shall not offer, sell, or deliver Grams to
16 any person or entity pending the hearing of the preliminary
17 injunction motion. Now on the day of the hearing, somebody can
18 stand up and ask for a continuation of that, somebody can ask
19 for a dissolution of that, but it seems to me you don't need
20 paragraph one at all, you don't need that.

21 Now the other items, three and four and seven, some
22 reservation of rights for both sides, and seven sounds always a
23 fine thing to do, it doesn't hurt, you probably reserve those
24 rights whether you put the language in or not. So that sounds
25 good.

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1 And let me see whether I can get you a date that would
2 work. I have a criminal trial starting the week of January 20
3 and a criminal trial starting the week of February 3rd, so I
4 would propose to have the briefing, the injunction hearing,
5 everything on February 17 at -- we'll begin on the 17th, we'll
6 begin at 11:00 a.m., and I'll set aside the 17th and the 18th,
7 if parties think that is going to be enough for the hearing on
8 the preliminary injunction. And the parties may, of course,
9 move or cross move for summary judgment.

10 The requirement would be that all the final last brief
11 of any sort by anyone on anything, that includes reply,
12 surreply, sur, sur surreply or any other denominated filing
13 would be in hand by January 27 so that the Court can adequately
14 prepare for the hearing.

15 MR. DRYLEWSKI: Your Honor, if I may.

16 THE COURT: Yes.

17 MR. DRYLEWSKI: Just one point, February 17 is
18 Presidents' Day. We're fine on that day, but if the Court
19 isn't open --

20 THE COURT: No, all right, thank you. We'll make it
21 the 18th and 19th. Again we'll start at 11:00 on the 18th,
22 we'll start at 10:00 on the 19th.

23 And what I'll do is I will keep the date we have on
24 now, which is the 24th, and I anticipate vacating that as soon
25 as I get a stipulation which lays out the schedule and includes

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1 what I call a standstill.

2 All right? Does that work for everybody?

3 MR. TENREIRO: Yes, your Honor. May I seek
4 clarification on one point?

5 THE COURT: Sure.

6 MR. TENREIRO: On the language of the standstill, I
7 think I understood the Court in terms of timing. What we would
8 request -- and we can take this back to defendants, we already
9 requested it -- language that says or "otherwise violates
10 Section 5," because I don't know that distributing Grams is the
11 only way that they can violate Section 5.

12 THE COURT: Here's the problem you have, and it has
13 been very much on my mind: You look at Rule 65(d) and the
14 Second Circuit's case law in this area, and a temporary
15 restraining order or preliminary injunction should describe the
16 act or acts restrained, and the Court has specifically
17 condemned an injunction which requires the subsequent
18 determination of whether a law has been violated.

19 Now I understand in consent injunctions that's done
20 every day, but those are consent injunctions, and the Second
21 Circuit noted specifically that point. So that's my problem
22 with Section 5.

23 Now I will tell you this, that you have the ability --
24 you need to reserve for your client the ability to come in on a
25 moment's notice if facts change. I am not foreclosing that

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1 possibility, and if something develops, I am sure you will be
2 here quite quickly.

3 MR. TENREIRO: Thank you, your Honor.

4 THE COURT: All right. What else?

5 MR. DRYLEWSKI: Nothing from the defendants, your
6 Honor.

7 THE COURT: All right.

8 MR. TENREIRO: Nothing from us, your Honor.

9 THE COURT: So I'm not anticipating seeing you on the
10 24th, but I'm holding that possibility open, and for the -- I
11 should say for the preliminary injunction hearing, it will be
12 done by direct testimony by affidavits. So you have to work
13 out a schedule on that for all witnesses under a party's
14 control.

15 MR. TENREIRO: Thank you, your Honor. Are we
16 permitted to put in any live testimony of a witness if the
17 witnesses are here and willing to show up and testify, or do
18 everything by affidavit?

19 THE COURT: If it's a witness who you can control,
20 they're coming voluntarily, then that should be direct
21 testimony by affidavit.

22 MR. TENREIRO: By affidavit.

23 THE COURT: If it's an adverse witness, then it can't
24 be, obviously. And you will find some guidance in my
25 individual practices on this. They spell out how this should

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1 be done. And the party with the burden of proof would go
2 first, then the defendants, and, of course, you have the right
3 to put in a rebuttal declaration as you would in any hearing.

4 MR. TENREIRO: Thank you, your Honor.

5 THE COURT: Okay. I think that's probably it.

6 Anything else from the defendants?

7 MR. DRYLEWSKI: Nothing, your Honor, thank you.

8 THE COURT: Thanks for coming in on very short notice,
9 I appreciate it. And I think this is shaping up to be a
10 sensible way to proceed. Thank you.

11 MR. TENREIRO: Thank you, your Honor.

12 MR. DRYLEWSKI: Thank you.

13 (Adjourned)